

# City Council Work Session

## Arts Education and Access Income Tax



Wednesday, July 24, 2013

OMF Revenue Bureau

1 of 39

# Agenda

- Framework for Work Session: Resolution 37007
- Current status update
- Next steps in administration of tax
- Equity as it relates to income tax fundamentals
- Options for Arts Tax changes
- Use of outside collection agencies
- Convenience fees (for using credit/debit cards)
- Equity outreach budget
- Intergovernmental agreements & RACC contract
- Arts Tax Citizen Oversight Committee and public outreach



# Council Resolution 37007

## Adopted March 27, 2013

- Directed Revenue to “submit recommendations to the Council... regarding proposed modifications to the Arts Tax to achieve Council’s directions on equity and fairness balanced with achieving the intended support for the arts and arts education.”
  - Numerous meetings occurred with Council representatives and Equity Director since March
- Directed that “any new tax structure for the Arts Tax should raise at least \$12-13 million in net revenues...”
- Directed Revenue to “submit a plan to address when a private for-profit collection agency may be contracted or assigned debt, including a provision that a debt cannot be assigned to such agencies until the debt reaches a minimum threshold to be later determined by the Council.”



# Current Status Update

- As of July 23, 2013
  - 252,919 tax filers
  - \$7,896,158 tax revenue
- Workload: 25,750 phone calls answered; 77,000 tax forms entered
- Estimated revenue reductions resulting from changes:
  - \* **\$12 million original revenue estimate for tax year 2012** (after “terminal compliance”)
    - “Lost revenue” since tax code enacted:
      - \$277,000 - \$700,000 income definition change (< \$1,000 not taxable)
      - \$500,000 - \$800,000 Social Security, railroad retirement (not taxable, state const.)
      - \$475,000 - \$600,000 PERS/FERS (not taxable, state/federal laws)
      - \$1.25 - \$2.1 million total estimated lost revenue**
  - \* **\$9.9 – \$10.8 million current revised estimate** (after terminal compliance)



*Terminal Compliance: Compliance rate after a full two-year cycle of non-filer identification and collection activity*



# Next Steps in Administration of Tax

- Refund notifications and forms will be mailed to approximately 125,000 households (July/August)
- Process refund requests (July/August/September)
- Identify taxpayers who did not file, a.k.a. “non-filers” (late August/September)
- Send non-filer collection letters (September and beyond):
  - Assesses a \$15 late penalty
  - Waives penalty if paid in 30 days



# Equity & Income Tax Fundamentals

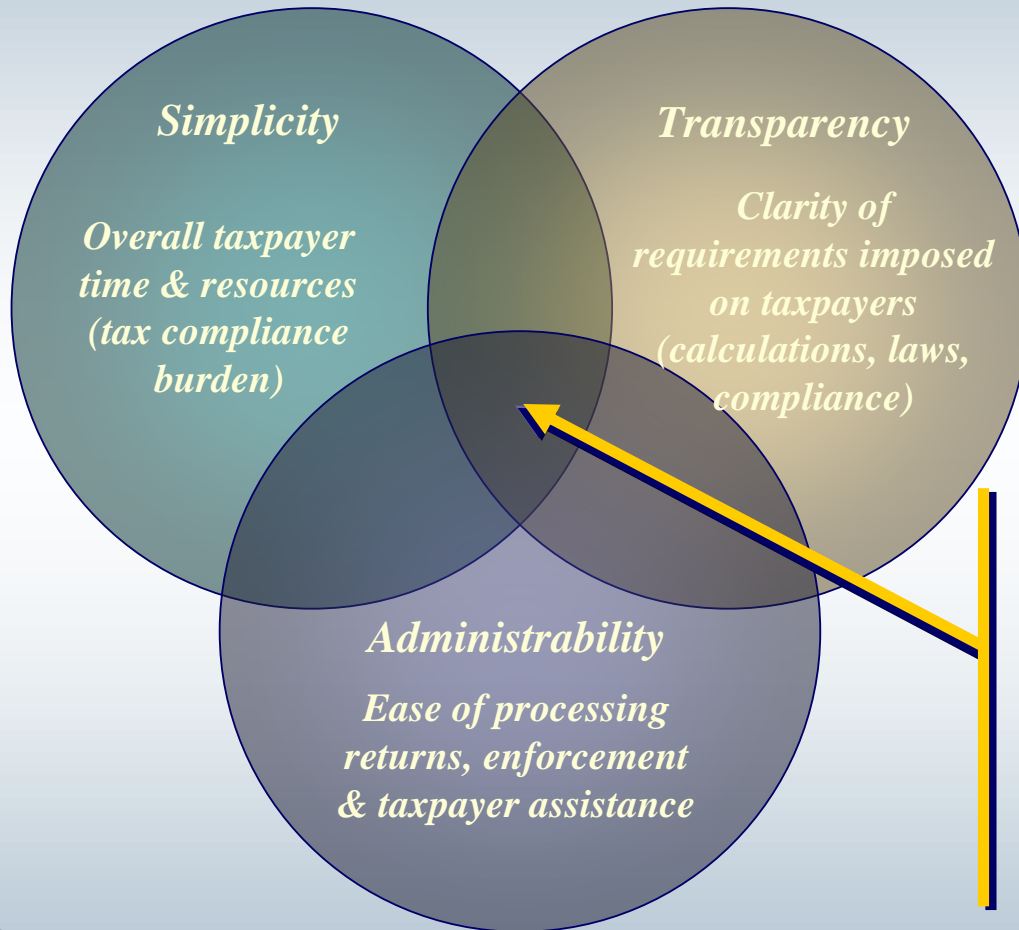
Summarized from “Understanding the Tax Reform Debate”, GAO, September 2005

## Some elements to consider when enacting income taxes:

- Ability to pay: those who are more capable of bearing the burden of taxes should pay more than those less capable
- The tax structure should produce the desired amount of revenue while balancing:
  - Administrative efficiency & cost of collection
  - Equity
  - Simplicity
  - Transparency



# Income Tax Fundamentals: Simplicity, Transparency & Administrability



Tax structures that balance simplicity, transparency & administrability reduce the total cost to the taxpayer



# Options: Arts Tax changes

- Option 1: Leave the tax “As is”
- Option 2A: Change to one bracket of \$50; increase poverty exemption
- Option 2B: Change to two brackets of \$35 and \$65; increase poverty exemption
- Option 3: Use Oregon Taxable Income (“OTI”) and three brackets of \$35, \$75 and \$100 (double for joint filers)
- Option 4A: Use OTI multiplied by a percentage tax (.15%) with a “floor” of \$20
- Option 4B: Use OTI multiplied by a percentage tax (.19%) with a floor of \$20 and “ceiling” of \$250

*Note – All options except “As is” recover lost revenue and provide \$12-13 million in net revenue as directed by Council*



*Oregon Taxable Income (OTI): federal gross income reduced by Oregon deductions*





# Option 1: Leave “As is”

- \$35 per income earning adult resident
- No tax is due if individual annual income is under \$1,000
- No tax is due if household is under federal poverty level (about 1/8th of adult population)
- Income from Social Security, SSI Disability, Oregon PERS, federal retirement and certain other incomes are not taxable (under any option)



# Option 1: Leave “As is”

## Examples of impact on a family of two adults and one child:

- Taxpayer scenario #1: each adult has income over \$1,000 and combined gross income of \$25,000
  - **Total Tax = \$70**
- Taxpayer scenario #2: each adult has income over \$1,000 and combined gross income of \$55,000
  - **Total Tax = \$70**
- Taxpayer scenario #3: each adult has income over \$1,000 and combined gross income of \$150,000
  - **Total Tax = \$70**
- Taxpayer scenario #4: each adult has income over \$1,000 and combined gross income of \$1,000,000
  - **Total Tax = \$70**

*The tax amount would be half if there was only one adult with income over \$1,000*



# Option 1: Leave “As is”

## Pros

- Closest to what voters passed
- Predictable (revenues, filing requirements, administrative procedures, problems/issues)
- Low burden for most filers
  - Least income verification of all options
  - Easy to pay (for self, others)
- No increased costs
- Upheld at Circuit Court level

## Cons

- Most regressive option
- Liability for many students (high school and college)
- Revenue projections reduced to \$9.9 million to \$10.8 million
- 5% limitation on administrative costs will no longer be met because of lost revenues
  - Requires a code change allowing costs to reach 6.5% of gross revenue



*Regressive tax: tax liability is a smaller percentage of a taxpayer's income as income increases*



# Option 2A: Change to one bracket of \$50; increase poverty exemption

- \$50 per income-earning adult resident
- No tax is due if individual annual income is under \$1,000
- No tax is due if household is under **200% of federal poverty level**
- Approximately 1/3 of adults would be exempt at this level; 2/3 would pay \$50
- Income from Social Security, SSI Disability, PERS, federal retirement and certain other incomes are not taxable

**How the exemption level would change based on the 2012 federal poverty guideline**

<i>Persons in Household</i>	<i>100% of Poverty Guideline</i>	<i>200% of Poverty Guideline</i>
1	\$11,170	\$22,340
2	\$15,130	\$30,260
3	\$19,090	\$38,180
4	\$23,050	\$46,100
5	\$27,010	\$54,020



# Option 2A: Change to one bracket of \$50; increase poverty exemption

## Examples of impact on a family of two adults and one child:

- Taxpayer scenario #1: each adult has income over \$1,000 with household gross income of \$25,000
  - **Total Tax = \$0**
- Taxpayer scenario #2: each adult has income over \$1,000 with household gross income of \$55,000
  - **Total Tax = \$100**
- Taxpayer scenario #3: each adult has income over \$1,000 with household gross income of \$150,000
  - **Total Tax = \$100**
- Taxpayer scenario #4: each adult has income over \$1,000 with household gross income of \$1,000,000
  - **Total Tax = \$100**

*The tax amount would be half if there was only one adult with income over \$1,000*



# Option 2A: Change to one bracket of \$50; increase poverty exemption

## Pros

- Predictable (revenues, administrative procedures, problems/issues)
- Remains simple for most filers
  - Little income verification
  - No federal or Oregon return required
  - Easy to pay (for self, others)
- No one-time cost increases
- Increased tax amount recovers “lost” revenue
- Can be implemented quickly

## Cons

- Regressive
- Liability for many students (high school and college)
- Possible continued legal challenges
- Additional 1.0 FTE and \$100,916 budget required for ongoing administration (exemption income verification increases)
- Requires a code change allowing costs to reach 5.8% of gross revenue



## Option 2B: Change to two brackets of \$35 and \$65; increase poverty exemption

- Same as option 2A, except individuals in households with gross incomes above \$75,000 pay \$65 (two adults \$130)
- Approximately 1/3 of adults would be exempt; 1/3 would pay \$35 and 1/3 would pay \$65



# Option 2B: Change to two brackets of \$35 and \$65; increase poverty exemption

## Examples of impact on a family of two adults and one child:

- Taxpayer scenario #1: each adult has income over \$1,000 with household gross income of \$25,000
  - **Total Tax = \$0**
- Taxpayer scenario #2: each adult has income over \$1,000 with household gross income of \$55,000
  - **Total Tax = \$70**
- Taxpayer scenario #3: each adult has income over \$1,000 with household gross income of \$150,000
  - **Total Tax = \$130**
- Taxpayer scenario #4: each adult has income over \$1,000 with household gross income of \$1,000,000
  - **Total Tax = \$130**

*The tax amount would be half if there was only one adult with income over \$1,000*





# Option 2B: Change to two brackets of \$35 and \$65; increase poverty exemption

## Pros

- Fewer low-income taxpayers required to pay
- New one-time costs are relatively small (\$50,000)
- Can be implemented quickly
- Remains simple for most filers

## Cons

- Different tax brackets creates:
  - More complexity for many taxpayers (calculating income, providing verification documents, etc.)
  - Additional 1.0 FTE and \$100,916 budget required for ongoing administration (exemption income verification increases)
  - Requires a code change allowing costs to reach 5.8% of gross revenue



# Options 3, 4A & 4B:

Move away from using household gross income and instead use Oregon Taxable Income (OTI) as the basis for computing the tax due



# Option 3: OTI with three bracket structure of \$35, \$75 and \$100 (double for joint filers)

OTI is used to allocate taxpayers  
to tax brackets



# Option 3: OTI with three bracketed structure of \$35, \$75 and \$100 (double for joint filers)

Arts Tax liability based on filing status (single, head of household, married filing separately, married or registered domestic partners filing jointly) & OTI as below

<i>Single, Head of Household, Married Filing Separately (OTI)</i>	<i>Estimated Number of Taxpayers</i>	<i>Arts Tax Amount</i>
No Oregon filing required	56,000	\$0
\$17,500 and under	82,000	\$0
\$17,501 to \$25,000	20,000	\$35
\$25,001 to \$35,000	18,000	\$75
Over \$35,000	23,000	\$100

<i>Married or Registered Domestic Partners Filing Jointly (OTI)</i>	<i>Estimated Number of Taxpayers*</i>	<i>Arts Tax Amount (Total)</i>
No Oregon filing required	56,000	\$0
\$35,000 and under	83,000	\$0
\$35,001 to \$50,000	37,000	\$70
\$50,001 to \$70,000	44,000	\$150
Over \$70,000	53,000	\$200



\*two taxpayers per filing

# Option 3: OTI with three bracketed structure of \$35, \$75 and \$100 (double for joint filers)

## Examples of impact on a family of two adult/joint filers and one child:

- Taxpayer scenario #1: combined OTI of \$20,000
  - **Total Tax = \$0**
- Taxpayer scenario #2: combined OTI of \$38,000
  - **Total Tax = \$70**
- Taxpayer scenario #3: combined OTI of \$100,000
  - **Total Tax = \$200**
- Taxpayer scenario #4: combined OTI of \$1,000,000
  - **Total Tax = \$200**

*The tax amount would be half if there was only one adult*



# Option 3: OTI with three bracketed structure of \$35, \$75 and \$100 (double for joint filers)

## Pros

- Less regressive
- Tax amount tied directly to a line on the Oregon tax return
- In general, high school and college students would not pay
- Income no longer needs to be compared to federal poverty guideline, a point of confusion under the current tax structure
- Increased tax amounts recovers “lost” revenue

## Cons

- Substantially different from what voters passed
- High taxpayer confusion the first year
- Filing requirements more complex and intrusive (requires federal/Oregon return, full SSN, etc.)
- Increased one-time costs
- Additional 1.5 FTE and \$169,359 budget required for ongoing administration (income verification increases)
- Requires a code change allowing costs to reach 6.4% of gross revenue
- Longer implementation timeline (TY 2014) with current resourcing, especially if referred to voters



# Option 4A: OTI percentage tax (0.15%) with “floor” of \$20

- Tax calculated at .15% of OTI
- If .15% of OTI is less than \$20 there is no Arts Tax due
- \$20 floor prevents taxpayers with low incomes from writing small checks
- Approximately 1/2 of adults would have no tax due



# Option 4A: OTI percentage tax (0.15%) with floor of \$20

## Examples of impact on a family of two adults and one child:

- Taxpayer scenario #1: combined OTI of \$20,000
  - **Total Tax = \$30**
- Taxpayer scenario #2: combined OTI of \$38,000
  - **Total Tax = \$57**
- Taxpayer scenario #3: combined OTI of \$100,000
  - **Total Tax = \$150**
- Taxpayer scenario #4: combined OTI of \$1,000,000
  - **Total Tax = \$1,500**





# Option 4A: OTI percentage tax (0.15%) with floor of \$20

## Pros

- Least regressive
- Tax amount tied directly to a line on the Oregon tax return
- In general, high school and college students would not pay
- Revenue Bureau experience in administering similar tax (Multnomah County ITAX)
- Income no longer needs to be compared to federal poverty guideline, a point of confusion for many taxpayers under the current tax structure
- Increased tax amounts recovers “lost” revenue

## Cons

- Substantially different from what voters passed
- High taxpayer confusion the first year
- Filing requirements more complex and intrusive (requires federal/Oregon return, full SSN, etc.)
- Relatively high new one-time costs
- Additional 1.5 FTE and \$169,359 budget required for ongoing administration (income verification increases)
- Requires a code change allowing costs to reach 6.4% of gross revenue
- Longer implementation timeline (TY 2014) with current resourcing, especially if referred to voters



# Option 4B: OTI percentage tax (.19%) with floor of \$20 and ceiling of \$250

- Tax is .19% of OTI
- If .19% of OTI is less than \$20 there is no Arts Tax due  
\$250 ‘ceiling’ to cap the tax amount paid for higher  
income families
- Approximately ½ of adults would have no tax due



# Option 4B: OTI percentage tax (.19%) with floor of \$20 and ceiling of \$250

## Examples of impact on a family of two adults and one child:

- Taxpayer scenario #1: combined OTI of \$20,000
  - **Total Tax = \$38**
- Taxpayer scenario #2: combined OTI of \$38,000
  - **Total Tax = \$72**
- Taxpayer scenario #3: combined OTI of \$100,000
  - **Total Tax = \$190**
- Taxpayer scenario #4: combined OTI of \$1,000,000
  - **Total Tax = \$250**



# Option 4B: Percentage tax based on OTI, floor & ceiling

## Pros

- Tax amount tied directly to a line on the Oregon tax return
- In general, high school and college students would not pay
- Revenue Bureau experience in administering similar tax (Multnomah County ITAX)
- Income no longer needs to be compared to federal poverty guideline, a point of confusion for many taxpayers under the current tax structure
- Increased tax amounts recovers “lost” revenue

## Cons

- Substantially different from what voters passed
- High taxpayer confusion the first year
- Filing requirements more complex and intrusive (requires federal/Oregon return, full SSN, etc.)
- Relatively high new one-time costs
- Additional 1.5 FTE and \$169,359 budget required for ongoing administration (income verification increases)
- Requires a code change allowing costs to reach 6.4% of gross revenue
- Longer implementation timeline (TY 2014) with current resourcing, especially if referred to voters

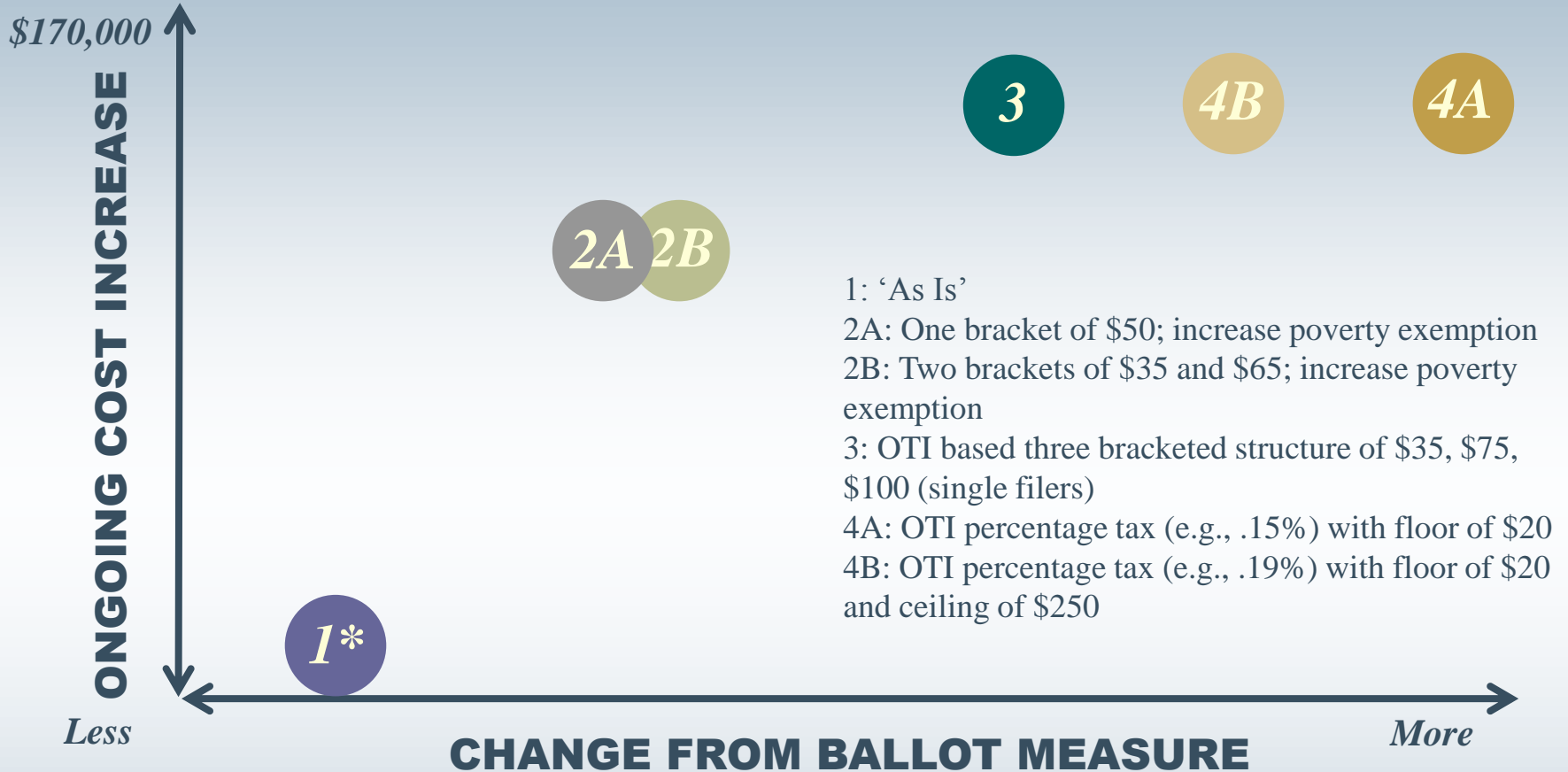


# Summary of Payers, Non-Payers, All Options and Scenarios

<i>Option</i>	<i>No Tax Due (estimated fraction of adult population)</i>	<i>Scenario #1 (Lower Income Family)</i>	<i>Scenario #2 (Middle Income Family)</i>	<i>Scenario #3 (Higher Middle Income Family)</i>	<i>Scenario #4 (High Income Family)</i>
<b>Option 1:</b> Leave 'As Is'	1/4	\$70	\$70	\$70	\$70
<b>Option 2A:</b> One bracket (\$50); increase poverty level	1/3	\$0	\$100	\$100	\$100
<b>Option 2B:</b> Two brackets (\$35 and \$65); increase poverty level	1/3	\$0	\$70	\$130	\$130
<b>Option 3:</b> OTI three bracket structure (\$35, \$75, \$100)	1/2	\$0	\$70	\$200	\$200
<b>Option 4A:</b> OTI percentage tax (0.15%), \$20 floor	1/2	\$30	\$57	\$150	\$1,500
<b>Option 4B:</b> OTI percentage tax (0.19%), \$20 floor & \$250 ceiling	1/2	\$38	\$72	\$190	\$250



# Ongoing costs & change from ballot measure

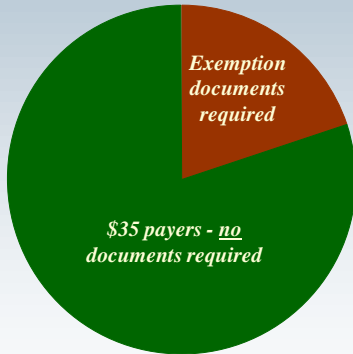


*\* City Council and legal challenges altered Option 1 from the original ballot measure*

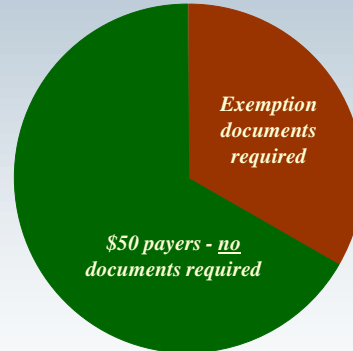


# Taxpayer burden: income verification requirements

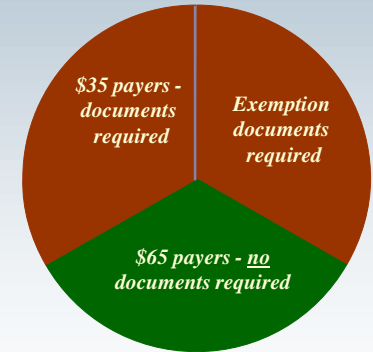
*Option 1 - Leave "As Is"*



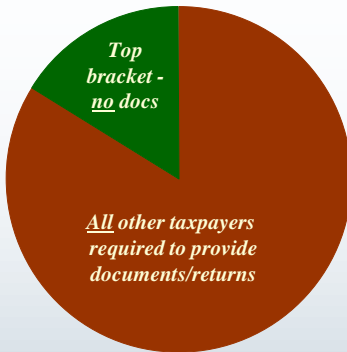
*Option 2A – Higher exemption/one bracket*



*Option 2B – Higher exemption/two brackets*



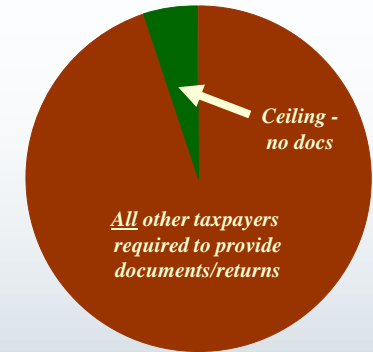
*Option 3 – Bracketed tax, OTI*



*Option 4A – % tax, OTI, floor only*









*Option 4B – % tax, OTI, floor & ceiling*



*Taxpayer burden: time and resources required for taxpayers to comply with the tax laws, including out-of-pocket costs*



# Bureau workload & budget changes

<i>Option</i>	<i>Bureau Workload</i>	<i>Budget Changes</i>	<i>Council Code Amendment Action</i>
<b>Option 1:</b> Leave “As is”	 No change	Reduced/revised revenue of \$9.9 million to \$10.8 million no budget change but cap exceeded	Increase cost cap to 6.5%
<b>Option 2A:</b> Increase poverty exemption, one bracket	 Increased income verification	Increase 1 FTE \$100,916; no change to one-time	Tax code; increase cost cap to 5.8%
<b>Option 2B:</b> Increase poverty exemption, two brackets	 Increased income verification	Increase 1 FTE \$100,916; increased one-time	Tax code; increase cost cap to 5.8%
<b>Option 3:</b> Bracketed tax, OTI	 Most taxpayers need income verification	Increase 1.5 FTE \$169,359; increased one-time	Tax code; increase cost cap to 6.4%
<b>Option 4A:</b> Percentage tax, OTI, floor only	 All taxpayers need income verification	Increase 1.5 FTE \$169,359; increased one-time	Tax code; increase cost cap to 6.4%
<b>Option 4B:</b> Percentage tax, OTI, floor & ceiling	 Almost all taxpayers need income verification	Increase 1.5 FTE \$169,359; increased one-time	Tax code; increase cost cap to 6.4%





# Implementation risk assuming September 4 Council action

<i>Option</i>	<i>Tax Year 2013 (Tax Due 2014)</i>	<i>Tax Year 2014 (Tax Due 2015)</i>	<i>Tax Year 2015 (Tax Due 2016)</i>
<b>Option 1:</b> “As is”	LOW	LOW	LOW
<b>Option 2A:</b> Increase poverty exemption, one bracket	LOW	LOW	LOW
<b>Option 2B:</b> Increase poverty exemption, two brackets	MEDIUM	LOW	LOW
<b>Option 3:</b> Bracketed tax, OTI	HIGH	MEDIUM	LOW
<b>Option 4A:</b> Percentage tax, OTI, floor only	HIGH	MEDIUM	LOW
<b>Option 4B:</b> Percentage tax, OTI, floor & ceiling	HIGH	MEDIUM	LOW



*Risk: identifying and assessing factors that may jeopardize the success of a project (budget, time, staffing, degree of change, etc.)*



# Collection Agency

- The 5% administrative cost cap drives the need to contract for collections after initial efforts fail
  - With 5% cap, Revenue has little capacity to pursue Arts Tax accounts that do not pay after two warning letters
  - Collection agencies add their fee on top of the amount owed
  - No cost to the City to refer to collection agencies
- Compliance rates and revenues significantly decrease without collection enforcement; revenue will be reduced if collection agencies are not used
- Ability to pay will be largely addressed by code change if options 2 - 4 are adopted
- Willingness to pay must be addressed by Bureau collection efforts and an outside collection agency unless budget is increased
- Accounts that remain without collection activity for 12-24 months are more difficult to collect
- The Bureau maintains full control of all accounts referred to the collection agency and can reclaim any account at any time using a secure web-based tool



# IRS & Oregon Department of Revenue Use of Collection Agencies; Bureau Recommendation

- The Oregon Department of Revenue (DOR) per ORS 293.231:
  - A delinquent income tax account shall be assigned by the DOR to a private collection agency if more than one year has elapsed without a payment on the account
  - The DOR may, at its discretion, choose not to assign a delinquent account to a private collection agency that is less than \$100, including penalties
  - The DOR may add a fee to the amount of the delinquent account
- The IRS does not use private collection agencies; it has extensive in-house collection infrastructure including wage garnishment
- Revenue Bureau recommends referring accounts to outside collections if they:
  - Owe greater than \$100 and are more than a year past due, or
  - Are two or more years past due



# “Convenience” Fee

- The Revenue Bureau currently charges a \$0.99 per transaction “convenience fee” for credit/debit card use to offset (in part) merchant fee charges levied by card issuers
- This measure was taken to ensure the 5% cost cap is not exceeded, but has proven unpopular with tax payers and is decreasing the online payment rate
- The City Attorney’s opinion is that merchant fees should “probably not” be counted as administrative costs based on the legislative history; recommends City Council clarify the code
- The Revenue Bureau recommends Council take action to exclude merchant fees charged by credit cards from the cap because they are beyond the control of the City and deter tax payers from paying online
- The Bureau can end the convenience fee charge paid by tax payers if merchant fees are not part of the cost cap



# Equity Outreach Budget

- There is currently no budget for:
  - Outreach to tax payers and vulnerable communities needing assistance
  - Additional explanatory mailing to all households
  - Additional outreach in print and web media
  - Expanded government partnerships (e.g., Office of Equity, ONI, TriMet, Multnomah County)
  - Printed materials in multiple language (website currently includes Spanish and more languages will be added)
  - Other outreach as identified by the Office of Equity
- Estimated \$100,000 needed to achieve above



# Intergovernmental Agreements & RACC Contract

- Payment schedule 11/15/2013 and 3/15/2014
- Council action required to change payment schedule



# Arts Tax Citizen Oversight Committee and Public Involvement

- Citizen committee has requested opportunity to review proposals being considered by Council
- Other outreach desired?

